

# City of Detroit


## CITY COUNCIL

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ANNE MARIE LANGAN  
DEPUTY DIRECTOR  
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TO: COUNCILMEMBERS

FROM: Irvin Corley, Jr., Director 

DATE: March 19, 2009

RE: City Council Fiscal Analysis Division Report on the December 31, 2008  
Quarterly Financial Report from the Budget Department

### **Introduction**

On March 10, 2009, the Budget, Finance & Audit Standing Committee received the Budget Department's Quarterly Financial Report for the period ending December 31, 2008. This report is required by court order. Attachment I is a copy of the report from the Budget Department.

The Quarterly Financial Report from the Budget Department is limited in scope as defined by the court order to five, actually currently four, major revenue sources and seven departments. One of the major revenues, State Equity Grants, is no longer included in the report as the grants have either been eliminated or go directly to agencies no longer a part of the general fund. The four remaining revenue sources represent 54.4% of the 2008-09 adopted general fund budget for revenues, and the seven departments represent 53.2% of the appropriations in the adopted budget.

The Fiscal Analysis Division's analysis updates the data through February 28, 2009, and includes an additional major revenue account, the Casino Gaming Fee. This increases the percentage of revenues reported to 66.6% of the adopted budget. Attachment II is the enhanced quarterly report data through February 28, 2009.

Included in this report is an update of the accumulated deficit through June 30, 2009 as reported in the city's financial reporting system.

### **Budget Department's Quarterly Financial Report for December 31, 2008**

In the cover letter of the report from the budget director states "Currently, we are projecting a shortfall of \$250 million." This is an increase of \$50 million from the previous report provided to Council for September 30, 2008. The basis of the projected shortfall includes reduced revenue collections, an increased 2007 deficit, and the absence

of the sale of fiscal stabilization bonds or a tunnel transaction taking place prior to the end of the fiscal year.

On the appropriation side the budget director is reporting appropriation surpluses as the result of vacancies. However, review of the Part II of the report from the Budget Department indicates year-end deficits in three of the seven departments included in the report.

In the report from the Budget Department, reference is made to a problem with encumbrances in the DRMS system, and that the remaining annual budget balance is inflated. **It would be helpful to the Fiscal Analysis Division for Council to request a written explanation detailing the actual problem including the magnitude of the problem, by agency and appropriation.** My analysis through February does not reflect any adjustment for this problem.

On the bottom of the "Part II General Fund Appropriations" section of the report from the Budget Department a note is made that fringe benefits for the entire general fund are estimated to result in neither a surplus nor deficit by the end of the fiscal year. The monitoring and estimate of a surplus or deficit in fringe benefit accounts is an important area for two reasons. First, the amount of fringe benefit costs incurred by the general fund. The 2008-09 Budget includes \$245.8 million for fringe benefits in the general fund, or 16.5% of the adopted budget. Second, due to the method of estimating, charging and year end reconciliation involved with fringe benefit accounts, it is impossible for the Fiscal Division to acquire accurate expenditure to budget data for this category during the year. Therefore an estimate on a quarterly basis from the administration would be a valuable addition for use in our projections.

Overall the Fiscal Analysis Division would concur that it is very possible that a \$250 million accumulated deficit will be reported by the city for the year ending June 30, 2009. In fact, our analysis of the financial reporting system updated through February 20, 2008 projects a \$254.5 deficit. See Table I – "Accumulated Deficit" below.

An accumulated deficit in the area of \$250 plus million will be very difficult to address in one fiscal period. It is our feeling that a more rational approach will require that a multi-year plan be developed along with a commitment to adhere to the plan over the years.

The more significant aspect of an accumulated deficit of \$250 million as of June 30, 2009 is the fact that the accumulated deficit continues to increase. This indicates that the structural budget problems within the city have not been addressed. Addressing the structural budget problem, or "balancing the budget" over a series of fiscal periods is the first step necessary to improve the financial status of the city. This must be done as a part of, or prior to addressing the accumulated deficit that has been building over the last several years.

## **Accumulated Deficit**

Table I – Accumulated Deficit (in millions)					
Line No.		Appropriations	Revenues	Net	Accumulated Deficit Estimate as of Dec. 31, 2008
1.	Accumulated Deficit as of June 30, 2007 - audited				\$(155.6)
2.	Prior Year's Deficit Appropriation included in 2007-08 Budget	\$88.6			\$(67.0)
3.	2007-08 Fiscal Year Results (un-audited) – General Fund	\$118.0	\$(184.9)	\$(66.9)	\$(154.7)
4.	Deficit Appropriation included in 2008-09 Budget	\$78.0			\$(76.7)
5.	Projected 2008-09 Results	\$73.8	\$(251.6)	\$(177.8)	\$(251.5)

## **Items for Consideration**

### **Fiscal 2007-08**

From our analysis it would appear that many closing and adjustment entries for the next fiscal period, fiscal year 2007-08 remain to be entered into the system. Our assumption is the majority of entries for the closing of this fiscal period have not been made, as the administration's efforts have been concentrated on completion of the audit for 2006-07. Some areas in the past that have resulted in significant movement in the final surplus/deficit number include, pension and fringe benefit charge adjustments, analysis of the risk management fund, subsidy requirements for "enterprise funds" like the Department of Transportation, Airport and Parking. Beginning with the 2007-08 fiscal period, we expect that shortages in the special purpose fund, the Solid Waste Fund, will be made up by the General Fund.

During our updating of the Quarterly Financial Report through February 28, 2009 on the appropriation side (Attachment II - Part II) of the report we discovered an item that requires an explanation from the Budget or Finance Department. In order to provide a comparison between the current year and prior year on the percentage of expenditures compared to the budget (column K of Attachment II) it is necessary that we review

previous period data in the system. When expenditures through February 2008, the prior period, were checked actual expenditures are reported as a negative \$3.6 million dollars. On the report this is reflected as a negative 20.26 percentage. **Again it would be helpful for Council to request a written explanation. It appears to be an error in the system that requires correction.**

## **Fiscal 2008-09**

Completing an estimate for the current year operations with a high level of confidence is complicated by the fact that previous fiscal periods have not been closed and audited. In general a major portion of our analysis relies on accurate reporting of prior year operations. Until these periods are closed the amount of collections and expenditures remain open to change that also would result in modification to our projections. In addition, the accumulated deficit remains somewhat of a moving target until the prior period(s) are closed. During our analysis of the current period, and in fact the 2007-08 period, it appears that recording of transactions may not be as consistent as we may have observed in the past. We would attribute this to the limited staff resources available to both complete past audits and maintain and review current operations, and the change in overall and financial management and the effort to gain a good handle on the financial status of the city in total. This should not be considered or taken as a criticism, as overall we believe a major effort is being made to improve the financial reporting of the city and provide financial statements in a timely manner. The purpose of the comment is to provide a good basis for understanding the projections and the confidence level that should be applied to them, and how they may defer from the past.

## **2008-09 Appropriations**

Using the raw numbers in the financial reporting system for the current year, as of February 28, 2009 and projecting out for the remainder of the fiscal year, with adjustments and assumptions, there is a potential for an appropriation surplus in the area of \$74.0. The assumptions relating to this estimate include: the actual recorded expenditures represent 66.6% of the total that is expected for the full year, the amount of encumbrances reflected as of February 28, 2009 will be expended by year end, an adjustment for the prior year deficit appropriation, and adjustments for major expenses that have not been recorded as of February.

An indication of how volatile this number is, by just changing the assumed percentage the February expenditures represent of the total from 66.6% to 61.6%, or 5%, the year end result would swing from the \$75 million appropriation surplus to a \$20 million deficit. Due to the cash flow situation the city faces, and the fact that vendor payments and other expenditures may be "managed" by the administration, this 61.6% assumption may be more accurate.

The holding of personnel requisitions and maintaining of vacant positions throughout the city along with the associated savings in benefit accounts may explain a portion of the projected appropriation surplus.

Implementation of a budget deficit reduction plan that includes significant savings in the current year would affect this estimate in a positive direction. But the more time that passes before implementation of any plan, the lower the savings will be during the current year.

## 2008-09 Revenues

2008-09 Revenue Projection Summary (in millions)	Projected June 30, 2009 Results, as of Feb. 28, 2009
Municipal Income Tax	\$(32.0)
State Revenue Sharing	(4.2)
Property Taxes	- 0 -
Casino Wagering Taxes	(21.0)
Utility Users' Tax	2.6
Sale of Property	7.0
All Other Revenues including Fiscal Stabilization Bonds	(204.0)
Revenue Total	\$(251.6)

Our analysis and projections of revenue accounts relies on past collection historical patterns along with comparison of year to date collections to year ending results. Again, not having previous fiscal periods closed and the potential that year ending adjustments and accrual entries remain to be recorded reduces the confidence factor for our estimates. For this analysis of revenues we believe it is important to keep in mind the overall economic conditions at the local, state and national levels. Revenue collections and projections that show decreases must be taken seriously and significant justification would need to be presented to even consider adjusting the estimates in a positive manner. The reality is that as citizens are facing employment reductions, business are reducing operations due to decreased demand, and other factors, revenue collections by the city are going to decrease.

Municipal Income Tax – Income tax collections recorded in the financial reporting system through February 28, 2009 are \$146.3 million compared to a budget of \$275 million. Over a five year period the February 28th collections of income tax represents around 60% of the year end total collection. Based on this assumption, net income tax collections could be as low as \$243 million for the year, or as much as a \$32 million deficit. The December 31st report from the Budget Department indicated a year ending deficit of \$20 million in income tax. However, that report showed year to date collections in December \$32.8 million worse than budget. The \$146.3 million in collections after eight months of the fiscal year is \$16.2 million lower than any of the previous six years.

Property Tax – Property tax collections through February 28, 2009, are \$121.4 million compared to a budget of \$177.5 million. At this point, through February, total recorded property taxes are \$56.1 million below budget. Since property taxes can be paid in total

in August, or half in August and half in January, collections after February, should represent nearly all of the anticipated collections.

After the second half of property taxes were due, in mid January, an increase in collections of only \$22.4 million is reflected in the system. This would indicate that a significant change in payment of property taxes has taken place, as historically the first half collections represent about 60% of total collections.

The total of property tax collections in December were \$99.0 million, a level that matched previous periods. Based on the \$99.0 first half collections, and the historical factor, year ending property tax collections could approach \$165.0 million.

This major difference in projection results raises our suspicion that there is either a delay in posting of property tax collections, or some other adjustment or correction remains to be made. In fiscal 2006-07, a similar low collection level was the result of a delay in the posting of collections.

Property taxes that are delinquent, unpaid in March of the fiscal year, are turned over to Wayne County for collection. The County of Wayne sells bonds and reimburses the city for these delinquent property taxes. Therefore, unless an adjustment for administrative costs of the program or for past taxes that are actually uncollectable by the County is required, property taxes collections can be expected to match the budget.

Wagering Tax – Per the regular monthly report of the gaming revenue at the end of February a \$21.0 million deficit is projected in this revenue.

Utility User Tax – Collections of the utility user tax through February is \$28.3 million. Using the year to date collections to the year ending total over the last five years an estimate of \$62.6 million in collection is projected, or a surplus of \$2.6 million. The Budget Department report indicates a \$5.0 million potential deficit in this revenue.

State Revenue Sharing – The collection of state revenue sharing by the city is dependant on two factors, the collection of sales tax by the state and reductions in revenue sharing by legislative action or executive order by the governor. At this point in time the state has not made any reductions in revenue sharing to local governments to address the State's fiscal problems, however that remains a possibility. We are in agreement with the Budget Department projection of a \$4.2 million deficit in revenue sharing collections.

All Other Revenues – The analysis of the collection of all other revenues remains an area that is very difficult to analyze as it represents a great number of individual revenue accounts that must be grouped together. The end of February analysis results in projections of large deficits in these combined revenue accounts. At this point we have judiciously adjusted the raw projection of these accounts to a \$126.0 million deficit. In addition the sale of fiscal stabilization bonds/tunnel deal or alternative at \$78.0 million combines to a total estimated \$204.0 million deficit.

## **Conclusion**

The most significant conclusion that can be taken from our analysis is that the city has not reached the point of balancing current revenues with current expenditures, the first step in improving the city's financial status. A first step that I am certain the rating agencies are waiting to see before any consideration would be given to an upgrade in the city's bond rating. Then, the next step, a workable plan to address the projected accumulated deficit of \$250.0 million, or even greater, will likely be expected by the bond rating agencies.

Even if it were possible to market fiscal stabilization bonds, the enabling legislation that allows the sale limits the amount to be sold to \$125 million. Based on the above analysis, the June 30, 2009 accumulated deficit could approach twice this amount. This means that this possible solution, one that would allow spreading the solution over a period of up to five years, can only address a portion of the problem without changes to the enabling legislation.

Looking forward to the preparation of next year's budget it is going to take a concerted effort to identify and fund only those critical services that the citizens cannot do without. While eliminating, transferring, or finding alternate funding sources for, those services that cannot continue to be provided or funded from general tax or revenue sources.

What can aid in the tough decision making is a cooperative effort, and working together attitude of those involved, the administration, legislative body, employees and bargaining units, and the understanding of the citizens. The ability of the city to spend beyond the amount collected in revenues must come to an end.

We look forward to and encourage questions and input from all Council Members and the administration, as we firmly believe open discussion and questions can only improve our ability to make projections in the future.

## **Attachments (2)**

cc: Council Divisions  
Loren Monroe, Auditor General  
Joseph Harris, Chief Finance Officer  
Pamela Scales, Budget Director  
Arese Robinson, Mayor's Office

CITY OF DETROIT  
BUDGET DEPARTMENT  
ADMINISTRATION

Budget, Finance & Audit  
Standing Committee  
Referred to Committee: 3-10-09  
LINE ITEM# \_\_\_\_\_ Date: \_\_\_\_\_  
Disposition \_\_\_\_\_

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## COMMITTEE

February 26, 2009

HONORABLE CITY COUNCIL:

**Re: Quarter Financial Report**

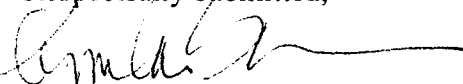
Attached please find the quarterly financial report for the period ending December 31, 2008. It should be noted that our financial system DRMS is reflecting a higher Remaining Annual Budget balance due to a system problem impacting encumbrance balances. This issue is being addressed by the Finance Department.

Currently, we are projecting a shortfall of \$250 million. This is essentially due to reduced revenue collections, increased 2007 deficit and fiscal stabilization bonds or tunnel transaction not occurring. We are however in the process of completing our comprehensive surplus/deficit estimate that will give more detail on our current operations. Vacancies in departments are generating appropriation surpluses and we continue to work diligently on all of our revenue collections and managing our cost.

We will continue to actively monitor expenditures and will provide your Honorable Body with an in depth departmental review of the 2008-2009 Budget in April. As in prior years, this information will be factored in the Mayor's Proposed Budget for 2009-2010.

I will be able to discuss this report, if necessary, at your convenience.

Respectfully submitted,



Pamela C. Scales  
Budget Director

cc: Joseph L. Harris, Chief Financial Officer  
Arese Robinson, City Council Liaison Mayor's Office



PART I  
GENERAL FUND  
MAJOR SOURCES OF REVENUE AND ESTIMATED SURPLUS/(DEFICIT)  
As of December 31, 2008

	Total Annual Budget	Amount Collected through 12/31/08	Better/(Worse) than Budget Year to Date	% Variance Better/(Worse) than Budget Year to Date	Remaining Annual Budget	% Collected to Date		Estimated Year End Surplus/(Deficit) Manually Computed
						Current Year	Prior Year	
Municipal Income Tax	\$ 275,000,000	\$ 104,676,128	\$ (32,823,872)	-23.87%	\$ 170,323,872	38.06%	46.87%	\$ (20,000,000)
Current Year Property Tax	177,469,000	98,976,322	10,241,822	11.54%	78,492,678	55.77%	48.21%	-
Utility Users' Tax	60,000,000	16,347,984	(13,652,016)	-45.51%	43,652,016	27.25%	25.93%	0 - (5,000,000)
State Revenue Sharing								
Sales Tax - Constitutional	\$ 63,596,394	\$ 23,475,378	\$ (8,322,819)	-26.17%	\$ 40,121,016	36.91%	18.26%	\$ 802,865
Sales Tax - Statutory	215,863,329	26,774,043	(81,157,621)	-75.19%	189,089,286	12.40%	16.54%	(4,955,858)
Subtotal	\$ 279,459,723	\$ 50,249,421	\$ (89,480,440)	-64.04%	\$ 229,210,302	17.98%	16.95%	\$ (4,152,993)
Total	\$ 791,928,723	\$ 270,249,855	\$ (125,714,506)	-31.75%	\$ 521,678,868	34.13%	35.11%	\$ 0 - (29,152,993)

Note: State Equity revenues were eliminated from the General Fund upon the transfer of the Zoo and Historical operations to an independent agency in FY 2006.

PART II  
GENERAL FUND APPROPRIATIONS  
(including fringe benefits)  
ESTIMATED SURPLUS/(DEFICIT)  
as of December 31, 2008

	Total Annual Budget	Amount Expended through December 31, 2008	Better/(Worse) than Budget Year to Date	% Variance Better/(Worse) than Budget Year to Date	Remaining Annual Budget	% Expended to Date		Estimated Year End Surplus/(Deficit) Manually Computed
						Current Year	Prior Year	
DEPT OF PUBLIC WORKS	\$ 11,935,713	\$ 4,503,203	\$ 1,464,653	24.54%	\$ 8,662,945	37.73%	78.74% **	(\$200,000) - \$600,000
FINANCE	41,111,960	19,489,058	1,066,922	5.19%	31,203,570	47.40%	44.08%	0 - 2,000,000
FIRE	187,195,995	101,276,242	(7,678,244)	-8.20%	88,886,155	54.10%	48.76%	(300,000) - 300,000
HEALTH	29,237,054	10,715,351	3,903,176	26.70%	21,699,412	36.65%	35.54%	1,000,000 - 2,000,000
POLICE	424,908,402	209,468,757	2,985,444	1.41%	228,038,169	49.30%	46.68%	0 - (2,400,000)
PUBLIC LIGHTING	64,827,195	34,247,377	(1,833,779)	-5.66%	55,788,849	52.83%	49.89%	(2,000,000) - (5,000,000)
RECREATION	28,751,182	11,082,628	3,292,963	22.91%	22,864,434	38.55%	30.90%	0 - 700,000
<b>TOTAL</b>	<b>\$ 787,967,501</b>	<b>\$ 390,782,616</b>	<b>\$ 3,201,135</b>	<b>0.81%</b>	<b>\$ 457,143,534</b>	<b>49.59%</b>	<b>46.93%</b>	<b>(\$1,500,000) - (\$1,800,000)</b>

NOTE: Fringe Benefits (entire General Fund, excluding pensions) are estimated to surplus/deficit in the amount of (\$0).

\*\* Beginning with fiscal year 2007-08, the Department of Public Works refuse collection activity is recorded in a separate fund, Fund 3104- Solid Waste

PART I  
GENERAL FUND  
MAJOR SOURCES OF REVENUES AND ESTIMATED SUPRLUS/DEFICIT  
for February 28, 2009, as of March 2009  
Prepared by the City Council Fiscal Analysis Division

Column Calculation	B	C	D C x %	E	F E - D	G F / D	H C - E	I E / C	J	
	Total Adopted Annual Budget	Total Amended Budget	Budget for Report Period 66.6%	Collected through Feb 28, 2009	Better/(Worse) than Budget Year to Date	% Variance Better/(Worse) than Budget Year to Date	Remaining Annual Budget	% Collected to Date Current Prior Year		Projected Year-End Results
Municipal Income Tax	\$275,000,000	\$275,000,000	\$183,150,000	\$151,811,460	(\$31,338,540)	-17.11%	123,188,540	55.20%	60.70%	(\$32,000,000)
Current Year Property Tax	177,469,000	177,469,000	118,194,354	121,354,387	3,160,033	2.67%	56,114,613	68.38%	85.92%	0
Utility Users' Tax	60,000,000	60,000,000	39,960,000	28,295,442	(11,664,558)	-29.19%	31,704,558	47.16%	45.49%	2,600,000
State Equity Package										
Historical	\$0	\$0	\$0	\$0	\$0	#DIV/0!	\$0	#DIV/0!	0.00%	0
Zoological	0	0	0	0	0	#DIV/0!	0	#DIV/0!	0.00%	0
Total	\$0	\$0	\$0	\$0	\$0	#DIV/0!	\$0	#DIV/0!	0.00%	0
State Revenue Sharing										
Sales Tax - Constitutional	\$63,596,394	\$63,596,394	\$42,355,198	\$23,475,378	(\$18,879,820)	-44.57%	40,121,016	36.91%	50.41%	800,000
Sales Tax - Statutory	215,863,329	215,863,329	143,764,977	26,774,043	(\$116,990,934)	-81.38%	189,089,286	12.40%	20.85%	(4,955,000)
Total	\$279,459,723	\$279,459,723	\$186,120,176	\$50,249,421	(\$135,870,754)	-73.00%	\$229,210,302	17.98%	27.81%	(4,155,000)
Grand Total	\$791,928,723	\$791,928,723	\$527,424,530	\$351,710,710	(\$175,713,819)	-33.32%	\$440,218,013	44.41%	53.62%	(33,555,000)
Casino Gaming Fee	\$194,780,000	\$194,780,000	129,723,480	\$117,941,194	(\$11,782,286)	-9.08%	\$76,838,806	60.55%	63.78%	(\$21,000,000)

PART II  
GENERAL FUND APPROPRIATIONS  
(including fringe benefits)  
for February 28, 2009, as of March 2009  
Prepared by the City Council Fiscal Analysis Division

Column Calculation	B	C	D C x %	E	F D - E	G F / D	H	I C-E-H	J E/C	K
	Total Adopted Annual Budget	Total Amended Budget	Budget for Report 66.6%	Amount Expended Feb 28, 2009	Better/(Worse) than Budget Year to Date	% Variance Better/(Worse) than Budget Year to Date	Encumbrances at Feb 28, 2009	Remaining Annual Budget	% Expended to Date Current	Prior Year
DEPARTMENT OF PUBLIC WORKS	\$11,935,713	\$14,928,258	\$9,942,220	\$5,759,303	\$4,182,916	42.07%	\$3,176,151	\$5,992,803	38.58%	-20.26%
FINANCE	41,111,960	46,803,083	31,170,853	24,996,301	\$6,174,552	19.81%	2,171,738	19,635,044	53.41%	55.20%
FIRE	187,195,995	187,239,120	124,701,254	127,786,640	(\$3,085,386)	-2.47%	1,142,034	58,310,446	68.25%	66.32%
HEALTH	29,237,054	30,555,190	20,349,757	14,550,955	\$5,798,802	28.50%	1,033,439	14,970,796	47.62%	47.23%
POLICE	424,908,402	429,326,350	285,931,349	272,290,869	\$13,640,480	4.77%	1,902,228	155,133,253	63.42%	60.45%
PUBLIC LIGHTING	64,827,195	68,895,949	45,884,702	44,614,250	\$1,270,452	2.77%	11,902,802	12,378,897	64.76%	68.18%
RECREATION	28,751,182	33,611,547	22,385,290	14,918,206	\$7,467,084	33.36%	2,564,072	16,129,269	44.38%	40.45%
	\$787,967,501	\$811,359,496	\$540,365,424	\$504,916,524	\$35,448,900	6.56%	23,892,463	282,550,509	62.23%	45.84%